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General Business Conditions

THE new year has begun quietly in business and the markets, and general economic conditions show no significant change. A seasonal resumption of operations has taken place in the industries which had curtailed output over the holidays, but new orders are light and have supplied no basis for any considerable expansion in productive activity. The automobile manufacturers have brought out new models which are agreed to represent the highest in quality and the lowest in price that the industry has ever offered; nevertheless, their sales expectations and factory schedules are both conservative. It is the opinion of the F. W. Dodge Corporation, statisticians of the building industry, that construction contracts awarded in the first quarter will be less than last year's figure by perhaps 15 per cent. Steel mill operations started off the year at 15 per cent of capacity, compared with 25 per cent at the beginning of 1932, and the seasonal increase during January has been slight, bringing the figure only to 18 per cent.

Retail trade has run behind a year ago by about the same margin as in December, the dollar sales of New York department stores in the first half of January having been 22.7 per cent smaller. In the primary textile markets buying has been light; however, the mills entered 1933 with order books better filled than a year ago, and textiles accordingly are more active than the heavy industries. The cotton mills had net unfilled orders at the end of December equal to nearly three weeks' output at that month's rate, and the rayon mills, which sold last year almost as much yarn as in their big year, 1931, are understood to have record bookings for first quarter delivery. These industries, and others making goods of everyday necessity, provide business with its chief support. They are keeping the general level of activity, as measured by the composite statistical indexes, substantially above the low point of last Summer, but of course the lack of employment in the heavy industries and the low farm purchasing power limit expectations of improvement.

The action of the security and commodity markets has been in line with the general quietness. Stocks and bonds have moved mostly sideways. Commodity prices on the whole have lost ground, but the chief farm cash products, wheat, cotton and livestock, have been firm or steady. The weakness has been in the petroleum group, silk, and some of the tropical products.

A Waiting Attitude

This brief description suggests that the general attitude is one of waiting for further developments in the situation, and undoubtedly this is the case.

Business men now recognize that on the monetary side a basis for recovery has been laid, in the check to deflation, and in the accumulation of idle capital and unused banking reserves in the money centers, ready for the needs of business when business can make profitable use of them. They recognize also that the process of working out a new equilibrium in the economic relationships that have been shattered by the depression is continuously going on: that costs and selling prices are being lowered, stocks of goods reduced, expenditures and incomes balanced, and debts which have become non-productive reduced or wiped out. They have witnessed, within the past six months, a vigorous and impressive demonstration of the recuperative power of the economic system, and realize that with cooperation and orderly adjustment the system will function normally again.

This is all ground for encouragement, but on the other hand there are a variety of less favorable conditions, which make it difficult or impossible to do business upon profitable terms. Readjustments are needed which require the cooperation of organized groups of people, or the action of governmental bodies, and neither is given as readily as is desirable. The burden of taxation is a barrier to cost reduction in all industry and agriculture, which the individual can do nothing to overcome except as his vote and personal influence may have effect. The country is not free from

agitation to alter the monetary standard or to debase the currency, and although both the President-elect and his party are pledged to sound money, and the Senate has summarily rejected by 56 votes to 18 a bill to remonetize silver, the agitation of these proposals interferes with the establishment of confidence. The strongest repudiation of inflationary ideas would be the balancing of the Federal budget, and this also would do most to revive the capital market and start the flow of funds to business again, but the Congress evidently will not balance the budget at this session.

One of the most disturbing of all the difficulties is the disorder in world trade and in currency relationships, which disrupts the exchange of goods between countries and exerts a constant pressure upon the price levels of commodities entering international trade. This is an economic problem vital to all countries; and it is in fact a series of separate problems, involving debts, tariffs and trade agreements, financial policies of governments, and other factors all intricately related. Any of these problems is difficult, and a harmonious treatment of the whole, opening a way back to a common standard of value, obviously will require the cooperation of all nations to the utmost possible extent, in a spirit of mutual concession and understanding.

Faced by these problems, and uncertain as to the action governmental bodies will take upon them, business men naturally hesitate to plan the expansion and replacement work needed to revive the heavy industries, and capital is timid; and this evidently governs the present situation.

Foreign Debt Conferences Arranged

In view of the paramount importance of the international currency disorder, and the obvious fact that the intergovernmental debts are a very serious obstacle in the way of stabilizing the exchanges and restoring a common standard of value, the decision of President Hoover and President-elect Roosevelt to cooperate in arranging meetings with representatives of the debtor countries, to be held in Washington soon after March 4, is the most important development of the month. This decision diminishes the possibility of another debt crisis, and brings discussion of the question nearer by many weeks than it could otherwise be held; and time is of great importance. It is the general desire to hold the projected international economic conference, in London, not later than May, but without preliminary discussion of the debt situation there evidently could be little hope of results from that conference. The step now taken confirms the position assumed by Messrs. Hoover and Roosevelt heretofore, that the debtor should have access to the creditor, and without this step it is unlikely that any other steps could be taken toward cooperative action for the purpose of terminating the currency disorder.

In the article upon the debt questions in the January issue of this Letter it was stated that "there is good reason to believe that the governments would adjust the differences by mutual concessions but for the pressure of public opinion against concessions," and undoubtedly public opinion will continue to be the decisive factor. The American people naturally want to deal with the situation in their own interest, and in formulating their opinions they should be sure where their chief interest lies. Incomparably it is in the restoration of trade and employment, and recovery in the price level. The instability of the exchanges is a principal factor in our domestic situation. It has been for some time past the major cause of the calamitous pressure upon prices of commodities moving in international trade; and these prices represent the purchasing power of a great body of American producers.

As long as the pressure on prices of raw materials lasts the wage cuts and other measures to reduce costs, and thus to bring the prices of manufactured goods into line with incomes and restore trade and employment, are largely ineffective. Throughout the depression the price of goods at retail and the cost of living generally has been declining, but in their downward course the prices in this group never have caught up with the drop in raw materials, and the disparities within the price structure have widened instead of diminishing. According to the report of the Department of Agriculture for December, the ratio of the prices of what the farmer produces to the prices of what he buys, standing at 50 per cent of the pre-war average, was the lowest of any month in the depression with the exception of June, 1932.

Effects of Unstable Exchanges

Evidently there is a general lack of understanding, even among business men, of the importance of having an international standard of value. Many have no conception of a world system of prices, of the influence that prices in one country exert upon the flow of trade and hence upon prices in another, or of the confusion which is inevitable when currencies no longer have any fixed relations to each other. They do not understand why we should lend our cooperation in restoring the gold standard, or even why we should maintain it ourselves, and this ignorance is the great element of danger today.

It must be considered that when the common standard is abandoned and the currency divorced from gold there is no barrier to a competition in depreciation among the various countries, and voluntarily or involuntarily the

countries move in that direction. In December the Union of South Africa suspended gold payments and allowed its currency to depreciate, and within the past month the government of New Zealand has altered the exchange rate on London from 9 to 25 per cent discount on sterling. This step was taken, the cables state, "in order to protect primary producers in New Zealand from a further fall in export prices." Stated in another way, this means that the exporters of New Zealand will be able to sell at lower prices in terms of gold, while receiving the same or a higher price in their own depreciated currency. Temporarily this may appear to be an advantage, but of course the depreciated currency will soon lose in internal purchasing power and the exporters will lose their apparent gain. Moreover, it is possible that other exporting countries may play the same game against New Zealand. Meanwhile a new and depressing competition is brought to bear against the world prices for wool, butter, meats and the other products which New Zealand exports, and naturally those products of the United States entering the world markets will be affected. The whole matter illustrates that limits of competitive currency depreciation can never be set; the only absolute limit would be the worthlessness of all currencies.

Under a condition of currency instability the transaction of normal business in accustomed channels may become practically impossible. In the discussion in our January Letter we gave several examples of the effects of depreciation of foreign currencies upon the trade of the United States, including the concentration of the world demand for wheat upon the Canadian, Argentine and Australian markets; a diversion of American ocean travel to Canadian lines; and the increase in imports of certain manufactured articles. Within the past month the cables have carried another striking example of the disturbance of ordinary business by the exchange situation, in the intervention of the British Treasury to stop the sale to British interests of 1,000,000 American-owned shares of the Boots Pure Drug Company, upon the ground that the resulting transfer of $25,000,000 to this country would upset the British exchange position. This contract had been entered into in good faith between the Liggett interests in this country and three London financial houses, and public offering of the shares prepared, when the Treasury intervened.

Some people may think Mr. Liggett's troubles only his own concern, but of course the same situation affects every effort of Americans to sell anything abroad, and that concerns a great many people, including farmers and manufacturers, those who sell to them, and those who are employed by them.

Incalculable Hazards

To the ordinary and calculable hazards of international business the lack of fixed relationships in the currencies adds fresh hazards. It makes transactions between parties in different countries a gamble, in which one party or the other must assume the risk of currency fluctuations, and of course it inflicts substantial losses in the normal course of business and investment. The London Times of December 21 contained a report of the annual meeting of Dorman, Long and Company, Ltd., the steel makers who had the contract for the new Harbour Bridge at Sydney, New South Wales, opened March 19 last. The chairman in his remarks referred to provision of the sum of £247,000 ($939,800) to cover a loss on that contract, which, made in 1924, was payable in Australian pounds, the company naturally not foreseeing that by 1931 the Australian pound would be worth only 16s. in London. On all the payments made since the exchange went to a discount the company of course has incurred a loss, and the deduction of the sum given follows another heavy deduction in the preceding year.

The losses of the British steel makers in the case given may seem, again, to be of no general concern, but it is evident that a normal international business cannot be transacted under such hazards. When trade is carried on under these conditions it is at the expense of prices. Moreover, the situation has provoked governmental interference with trade in an unprecedented degree, ranging from the exchange controls, which make impossible the transaction of business beyond the limits of the amount of exchange supplied by the controlling authority, to the tariffs and other forms of trade obstruction called into operation by these abnormal conditions. An illustration of the effects may be found in recent quotations of livestock in the Argentine markets, where heavy steers have sold as low as the equivalent of 1 cent a pound, and choice young steers at 1.8 cents. The principal explanation is in the meat trade provisions of the Ottawa agreement, which are designed to stimulate production within the British Empire at the expense of the present sources of supply.

Policies of This Country

The United States is affected by the situation we have been describing as much as any other country, and the distress in this country makes it imperative to seek relief from it. What policies are open to the United States, and what hope of relief do they afford? Some believe that we can ignore the rest of the world, allow our exports to dwindle continuously while shutting out imports by tariff walls, give up the expectation of receiving

payment on the debts due to us, and in short isolate ourselves into a self-contained economic system of our own. But we cannot believe that those who propose this have any conception of the disturbance in agriculture and the industries that would be caused by an attempt to live within ourselves, or of the long and costly readjustments that would be required. In our opinion this proposal offers no practicable way out of the confusion.

Others propose that we meet the depreciation of other currencies by the depreciation of our own, but they can have no conception of the futility of such action, or of the disaster that would result if all the remaining elements of order and stability in the situation were abandoned. We give a discussion of the money question subsequently in this Letter.

Against these impracticable proposals, offering no hope of anything but continued depression, may be set the advantages of a program of cooperation and mutual concession in dealing with the causes of the trade disorder and currency confusion; and of measures that would rouse confidence rather than alarm in capital and put the idle currency and credit in the country to work. The items in such a program undoubtedly would include an adjustment of the intergovernmental debts to assure that the exchanges may be free as long as necessary from the pressure of these great one-way payments; reduction of government expenditure and taxation; balancing the budget of the Federal and local governments; and adjustments of wages and prices in places where an adequate adjustment heretofore has been hampered or blocked.

We are aware that such a program lacks the appeal to an impatient and distressed people which accompanies the extraction of a white rabbit from a silk hat, and that the world would greatly prefer to have the depression overcome by the white rabbit method. But there is no practicable way of reviving the exchange of goods and services which constitutes business except by restoring terms upon which they will exchange, and by removing the obstacles to their exchange. Contrary to a common belief, such a road out of the depression need not prove to be a long one, for undoubtedly adjustment of the debts and balancing the Federal budget alone would vigorously stimulate the markets; and upon the foundation of confidence thus created the cost reductions and other factors of improvement to which business has applied its efforts during the depression would have an effect now denied them, under the present conditions of disorder and uncertainty.

Industrial Corporation Profits in 1932

The reports of corporate earnings for 1932 now being made public reflect in full degree the decline in the volume of business and in prices which took place during the year. A preliminary summary of the reports of 375 industrial corporations, for the fiscal or calendar year 1932, shows a combined net profit after all charges but before dividends, and after deducting the deficits, of $56,000,000 compared with $225,000,000 for the same companies in 1931, representing a decline of 75 per cent.

Deficits for the year were shown by 55 per cent of the reports tabulated to date, and aggregated $151,000,000, while in 1931 deficits were reported by 36 per cent and aggregated $97,000,000. A few companies did better in 1932 than in 1931. Our records show 52 concerns reporting an increase in profits, or a deficit changed to a net profit, but for the most part these companies are relatively small and not the leading and representative organizations in their respective industries. A sizeable group operated at a deficit both years, but decreased the size of the loss in 1932 compared with 1931.

Two features of the 1932 statements are the reduction in merchandise inventories and the retirement of bonded debt. The decrease in these two items since 1929 has been particularly marked. A group of 80 important industrial corporations having a net worth of $5,000,000 and upwards carried aggregate inventories at the end of 1929 of $900,000,000, which had been reduced to $639,000,000 at the end of 1931 and to $523,000,000 at the end of 1932, or a reduction of 42 per cent below 1929. An important part of the decline is accounted for by lower prices, while the remainder reflects the working down of stocks and the lower volume of business now being handled. Of the same group of important companies, 37 had funded debts, which aggregated $454,000,000 at the end of 1929, $418,000,000 in 1931 and $364,000,000 at the end of 1932, or 20 per cent below 1929. This retirement has come about through payments at maturity, serial maturities, calls for redemption, purchases for sinking funds, purchases in the open market (often at heavy discounts) and, in some cases, through scaling down debt through reorganizations.

Money and Banking

The piling up of funds in the principal money markets of the country has continued during January, carrying the surplus reserves of the banks to levels higher than ever before.

Monetary gold stocks increased $51,000,000, largely due to gold imports, while redeposit of currency in the banks after the Christmas trade amounted to $76,000,000. Since the increase in reserves had no counterpart in the demand for credit, the gain simply added to the excess of reserve above legal requirements, which now amounts to above $500,000,000.

The Further Reduction of Interest Rates

The influence of these huge supplies of funds was seen in the further reduction of interest rates, already unprecedentedly low, to almost the vanishing point. Bankers' acceptances were cut by ⅛ to ⅜ of 1 per cent bid, ¼ of 1 per cent asked for maturities up to 90 days, prime commercial paper was quoted at 1¼ per cent, and Stock Exchange time loans at ½—¾ per cent. Yields on Government short-term securities were a shade higher, but even so were quoted at the ridiculously low figures of .09 to approximately ½ of 1 per cent for maturities up to a year.

These conditions as to interest rates, together with the impossibility of finding employment for the available funds even at these unremunerative levels, led to action by the New York Clearing House to reduce the rates paid on deposits. Heretofore, no change had been made in these rates since May 13 last, during which time other short-term interest rates have undergone successive reductions. In posting the new schedule of rates to take effect January 25, the Clearing House also announced a change in the definition of demand and time deposits for purposes of calculating interest, ruling that henceforward demand deposits would include deposits repayable within 90 days instead of 30 days, as formerly.

Following is a schedule of the new Clearing House rates compared with those in effect previously:

Kind of Deposits	New Rate	Former Rate
	Per Cent	
Demand deposits of banks and trust companies	¼	½
Demand deposits of mutual sav. bks. in comm'l banks	½	1
Demand deposits of others	¼	½
Time deposits	½	1

Reserve Banks Reduce Government Security Holdings

Action of the Federal Reserve Banks in permitting approximately $88,000,000 of their Government security holdings to run off without replacement during the month constituted an interesting development. The reduction marks the first important decrease in these holdings since the Reserve banks began their policy of accumulating Governments in the Fall of 1929 just after the stock market crash of that year. At that time this policy was undertaken in the interest of easing the money market and facilitating liquidation. By the middle of 1931 holdings had been built up to approximately $600,000,000, whence they were later jumped to $1,850,000,000 during the Spring of 1932 when heavy purchases were made by the Reserve banks for the purpose of putting Federal Reserve funds in the market to offset the loss to member bank reserves caused by gold exports and the domestic hoarding of currency.

With the turn in the tide of gold and of currency hoarding about the middle of last year, additional purchases ceased. The Reserve banks, however, did not reduce their holdings, and as a consequence chiefly of continued gold imports, member banks reserves were rapidly built up to levels higher even than before the panic. By the end of the year it was apparent that a continuation of gold imports and the expected seasonal return flow of currency would bring about conditions in the money market justifying some action on the part of the Reserve bank authorities in reducing their large holdings of Governments. On January 5 the Federal Reserve gave first indications of a possible move in this direction in a public statement defining the objective of Reserve Bank open market policy as follows:

> The first and immediate objective of the open market policy was to contribute factors of safety and stability in meeting the forces of deflation. The larger objectives of the System's open market policy, to assist and accelerate the forces of economic recovery, are now assuming importance.
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> With this purpose in mind, the Conference has decided that there should be no change in the System's policy intended to maintain a substantial amount of excess member bank reserves, the continuance of which is deemed desirable in present conditions. Adjustments in the System's holdings in the open market account will be in accordance with this policy.

Following this statement occurred the successive weekly reduction of Reserve bank holdings of Government securities that has been referred to. It is evident, from the statement, however, that these reductions do not represent any alteration of fundamental policy on the part of the Reserve banks, which still propose to "maintain a substantial amount of excess member bank reserves" in order to "accelerate the forces of economic recovery."

Action of the Reserve banks in reducing their Government holdings had only slight effect on the Government market. Prices of shorter maturities have been a shade weaker, but those of longer maturities, after some temporary unsettlement, recovered and in some cases reached new high levels.

Proposals for Inflation

There is something incongruous in demands for monetary inflation as a means of correcting alleged instability in the gold standard, for certainly inflation by such crude methods as printing money in sums of billions, or an offhand reduction of the unit of value, give promise of anything but monetary stability. Most of the proposals make no pretense to a calculated control of money or prices; their advocates differ in billions upon the amount of inflation they desire to inject into the monetary system, and the projects are as vague and speculative as the wildest kind of a promotion scheme, yet they have to do with the money of the country, which is the basis of all business calculations, the measure by which

wages, incomes and savings are valued, and acknowledged to be of vital importance in the economic life of the nation. Surely, if there is to be any legislation affecting the standard of value in use there should be a more scientific preparation for it than is contemplated in these haphazard proposals. Emphatically is this so in view of the arrangements for a world conference by the nations this year for the purpose of considering coordinate action upon this and related subjects. The United States, through President Hoover, is pledged to participation in this conference and representatives of our Government have taken part in preparing the agenda. The state of disorder in the monetary exchanges is recognized to be the most important reason for holding the conference.

The arguments for inflation summed up briefly are that more money is needed in circulation and that something must be done to raise the level of prices, to the end that the purchasing and debt-paying power of the people shall be restored. The objectives unquestionably are desirable, but has the depression been due to lack of currency or can it be overcome by additions to the currency supply?

To name scarcity of money in circulation as a cause of the depression is to put the cart before the horse. Money circulates through the activities of business—buying, selling and the employment of labor. In 1929 about 56 per cent of the aggregate income of all the people of the United States was received in the form of wages and salaries. Another important population group is the farmers, among whom money circulates in exchange for their products. Money circulates to everybody who has something to sell and away from him when he expends it. As it finds its way into stores or other places of business, it is returned to the banks to go the rounds again. But under normal conditions nobody is supposed to receive money without giving something for it.

Since 1929 business has been seriously disorganized by a disruption of price relations between the products and services of different sections of the economic system, with the result that the flow of these offerings into consumption has been very much disturbed. As a result of these conditions products have accumulated, prices have fallen, unemployment has resulted and of course the amount of money moving in circulation has declined.

The Supply of Means of Payment

That there has been no lack of facilities for making payments is evident from the figures for the amount of lawful money of various forms outstanding since 1929. There is as much money in the country now as there was then and the gold reserves which are the basis of currency issues and bank credit are larger than then. Within the last year the provisions of law under which the Reserve banks issue credit and currency have been enlarged and the authorities, in the exercise of the new discretion allowed them, have purchased over $1,110,000,000 of Government securities in the public market, issuing Reserve credit in payment, all of which immediately entered the reserves of the banks doing business with the public. In the last eleven months the Reconstruction Finance Corporation has made loans aggregating over $1,600,000,000, additional national bank-notes to the amount of $144,000,000 have been issued under the Borah amendment to the national bank act, and something over $600,000,000 of gold has been imported since the middle of June.

The advocates of inflation wave aside these additions to the available supply of means of payment by saying that they do not constitute money in circulation. This is true. The amount of money in circulation on December 31, 1931, was $5,646,772,888, on December 31, 1932, $5,676,183,214 and on January 18, 1933, $5,602,000,000, the drop between the last two dates being due to the falling off of trade after the holidays. The latter change illustrates the dependence of the volume in circulation upon the volume of business. Nevertheless, deposits constitute the most important part of the available means of payment. The tens of billions of active bank deposits circulate through the checks being constantly drawn upon them, and also serve as a reservoir from which streams of currency flow out for payrolls, moving the crops and all the other uses of currency in circulation.

It is true, however, that neither deposits nor money can be effective upon prices unless used as purchasing power, and this use is practicable on a large scale only in the normal activities of industry and trade. As we have seen, there is plenty of money available for business, in the usual channels. The Government may flood the banks with money without any result beyond adding to the surplus, unless there is a revival of trade.

The only way money can be made to flow to persons who are out of employment or whose products have declined in purchasing power, is by some kind of forced circulation, i.e., by gifts, loans, or public works. Such a proposal raises no question as to the adequacy of the money supply in the usual sense, but since it is obviously impossible for the Government to raise the sums required for large scale operations of this kind by loans and taxation, proposals arise for printing money for the purpose.

Inflation as a Stimulant

In addition to the arguments in favor of the specific expenditures proposed it is urged that "moderate" issues of currency would give a stimulus to industry and also an upward start to prices. This argument is based upon a number of fallacies. In the first place the direct effects of the expenditures upon employment and prices would be negligible unless the currency issues were on such a scale as to soon falsify the promise of a "moderate" policy and inaugurate an utterly reckless policy. Second, it is a fallacy to assume that a mere issuance of more money will cause prices to rise. We have seen that such issues flow into the banks, and it is agreed that only money or bank credit in use as purchasing power can produce the desired results. This means that nothing will aid employment or prices but a revival of private enterprise and of self-supporting industry and trade. The will to use money must be strengthened, and there must be such a change in the outlook as will inspire confidence throughout the business community that fundamental conditions are sound.

The printing of money for the purpose of meeting a deficit in the Treasury budget, whether caused by relief legislation or otherwise, is universally recognized as unsound policy. The management of a credit currency is a delicate function which should be strictly confined to a skilled organization, such as the Federal Reserve system, which is a part of the banking system through which as we have seen most payments are made, and the issues should be strictly confined to supplying the circulating medium for business, and not involved in Treasury finances. This is a principle from which there should be no deviation, because such issues for extraneous purposes inevitably derange the monetary system, and once the door is opened to easy money for such uses, there is no effective control.

Every experiment of the kind is dangerous, because the allurements of easy money are great. History is full of warnings against such experiments and enough is known of them to inspire alarm in the minds of informed and prudent persons the moment a proposal appears likely to be adopted. The natural reaction was seen in the world panic which occurred in the last half of 1931 and first half of 1932, when one-half of the nations were forced off the gold basis and the United States lost over $1,000,000,000 of gold which had been deposited or employed here by foreign investors or bankers. The cause of the panic was fear that with the abandonment of the gold standard by so many countries a universal era of inflation would follow, and the result was that prices of commodities and of all kinds of property, instead of being stimulated by the prospect, sank to a state of depression seldom if ever previously known.

It is true that foreign deposits and investments in this country have been largely reduced, but a very substantial body of long term investments remains, and it would be impossible to calculate the attitude of our own people if inflationary legislation actually became imminent. The avowed object being to depreciate the currency it may be assumed that the policy would not stop short of forcing the country off the gold basis, for there is little reason to think that any effect upon prices or business would be had short of that. The policy would inspire distrust instead of confidence. Business men will not start up industries without feeling some assurance that they can operate without losses. The present situation is that the disruption of price relations, which is particularly marked between primary and finished goods, renders a normal volume of trade impossible. This situation can be changed only by readjustments in trade relationships, which mere additions to the stock of money in banks would not do.

Human nature responds to like conditions in very much the same way at different times, and this has been true in experience with paper money. If the country should be forced off the gold basis and the policy was carried far enough, depreciation doubtless would become manifest in rising prices, but not, there is reason to believe, in uniform effects, or orderly, enduring prosperity. The kind of rising prices that results from a fluctuating and depreciating currency does not make for general and sound prosperity. It affords no sure basis for business. It promotes speculation and eventually a stage of depreciation is reached which prompts the people to quickly exchange their money for anything rather than keep it. Inflation does not create uniform or calculable results. It is a speculative, reckless, irresponsible policy, a policy of desperation.

Mr. Henry J. Haskell, editor of the Kansas City Star, in a special article on the subject has described the psychology of it very well in a paragraph, as follows:

> Primarily inflation is like a balky and unruly horse. It simply refuses to be guided by the rider. At first it balks. The rider applies whip and spur and still it will not budge. Then of a sudden it bolts and there is no controlling it. When it finally stops it throws its rider and he is left flat on the ground.

It may be added that differing conditions attendant upon the inauguration of inflation affect the public attitude at the time. In war time, when a nation's attention and energies are fixed on the national effort and the demand for money and men is unlimited, inflation in the form of the usual means of payment is unnoticed, or accepted as a necessary incident of the situation, as in our own case, when everybody was urged to borrow for the purchase of Liberty bonds. The conditions of that situation favored the ready acceptance and use of additional means of payment. There

were no unbalanced relationships or other dragging influences in the business situation to nullify its effects. In the present state of stagnation, inertia, pessimism and disorder there is neither the incentive nor the opportunity to use increasing means of payment.

There are memories of the war inflation which should be a warning now. The Federal Reserve authorities are bitterly denounced to this day for not having found some way to continue increasing the issues of credit two years after the war had ended and when the expansive capacity of the system had reached the limit fixed by the Reserve Act. The demand for inflation is never satisfied.

The Debtor-Creditor Situation

The chief argument for inflation is based upon the present plight of debtors, which is due in part to the low level of commodity prices and in part to the stagnation in business. In the case of the railroads, industrial corporations and business men generally, the latter cause is the more important and there is reason to believe that if the economic system were brought back into balanced relations, so that goods and services would pay for each other in a normal way and enter freely into consumption, prices would make a decided recovery. It is important to distinguish between the rising prices which always result from orderly prosperity and rising prices which simply represent depreciating money. The former is what we want. The latter is a cheat to everybody who receives it and the resulting disorders are likely to nullify even the expected gain to debtors.

No matter how much some prices or even the general level might be raised by inflation, if the present disparities among prices continued and consumption did not increase, the results certainly would be disappointing to debtors. Everybody must make a living before he can pay debts, and it is noteworthy that even now, despite the great decline of prices in the last three years, the cost of living as officially computed is still about one-third above what it was in 1913. The prices of the staple products to which debtors look for relief have not been sustained in line with the cost of living, and unless there is a change in the supply and demand situation regarding these there is not likely to be much buying of such products for the future, regardless of the supply of money.

Agriculture did not share in corresponding degree with the revival in the other industries after the slump of 1920-21, but remained below parity with them, because supply and demand conditions nullified the natural influence of a general revival. At last the farmers must look to supply and demand conditions.

Also, unless the Government is to print enough money to pay all debts outright, the subject of renewals or extensions will be an important one, especially so with the future of the currency in a state of great uncertainty.

Effect of Inflation Upon Wages

A matter of large importance is the probable effects upon wages. Depreciation of the currency has been advocated in many countries as a painless method of reducing wages, wage-earners being placed on the defensive, in that they must obtain continual increases in order even to hold their own. It is urged that wage reductions are necessary in order to restore the equilibrium in industry, and that the workers will accept them more readily in the form of a depreciated currency than by rate reductions in the money of higher purchasing power. This may be so, but no uniform rule can be assumed.

An interesting situation illustrating this case exists in the Union of South Africa, where gold-mining is a great industry. Since the departure of Great Britain from the gold basis the mining companies have advocated that the Union adopt the same policy, attaching its "pound" to the British pound sterling in the former gold standard relationship. The effect of this would be to enable the companies to sell their gold at a premium now equal to about 30 per cent over the local currency, in which wages are paid, and if wage rates remained unchanged this would be clear gain to them. The argument of the companies frankly admitted that they would gain, but urged that living costs probably would not rise so much, and further that wages had been very much increased during the war on account of the higher living costs and had not been reduced in correspondence with the fall of living costs, also that lower operating costs would assure more employment by enabling the companies to work large bodies of low grade ores which now are left in the mines.

The Government declined to consider the proposal, but in December a split occurred in the party in power, the farmer element adopting the idea of going to the sterling standard. This action started a run on the banks for gold or foreign exchange, and the Government was forced to suspend gold payments. The situation is still unsettled, but the probabilities seem to be that the sterling standard will be adopted. Already the miners' union has presented a demand for a general wage increase of 35 per cent.

Nothing definite can be foretold about the effects of inflation upon wages, except that rate increases would be necessary to maintain the same purchasing power and that confusion inevitably would result.

There is, however, a very definite and very great risk to the wage-earning class in any movement for inflation, because all experience has shown that once such a movement is begun there is no knowing where it will stop. If the results at first are disappointing, the advocates always assume that the dose should have been stronger and proceed to increase it. When conditions become adjusted to inflation and the policy really gets into a stride, the doses must be repeated as fast as the effect wears off, until, as in all the booms, nobody wants it to stop or knows how to stop it, until it crashes in ruin. In all such experiences the wage-earners have suffered pathetically, not only in the shrinking value of their wages, but in the loss of savings in bank accounts, securities and life insurance. The labor leaders of every country on the continent of Europe give warnings against inflation as the wage-earners' worst enemy. Mr. Owen D. Young was profoundly impressed when he visited Berlin as a member of the Dawes Commission, by the statements made to the Commission by the labor leaders of Germany, describing the disadvantages and hardships under which the workingmen and their families had suffered through the depreciation of the currency.

The right way to settle the wage question is by facing all the facts frankly and seeking the basis of relationships between the various industries which will enable goods and services to be readily exchanged.

The French Assignats

The French working class suffered from currency depreciation during the last war and years following as did the workers of Germany, but France had an earlier experience of the same kind under the revolutionary government in 1790-96. That chapter of history is famous, and has been graphically told by a man of the very highest qualifications for appraising all of the circumstances related to it, the Hon. Andrew D. White, for many years President of Cornell University and later United States Ambassador to Germany.

The revolutionary government was receptive to so-called "progressive" ideas, and adopted a plausible scheme for a new monetary system. It had confiscated large holdings of lands from the Church, and these lands were assigned as security for the proposed currency issues, hence the latter became known as assignats. The outstanding currency besides being a legal tender was to draw interest at 3 per cent, which was thought to be security against an over-issue. The system broke down utterly, the issues finally reaching such an enormous aggregate that they became worthless. The following brief extracts from Dr. White's account of the system sum up the story:

> New issues of paper were clamored for as more drams are demanded by a drunkard. New issues only increased the evil; capitalists were all the more reluctant to embark their money on such a sea of doubt. Workmen of all sorts were more and more thrown out of employment.
>
> * * * * * *
>
> On the 18th of February, 1796, at nine o'clock in the morning, in the presence of a great crowd, the machinery, plates and paper for printing assignats were brought to the Place Vendome and there, on the spot where the Napoleon Column now stands, these were solemnly broken and burned.
>
> * * * * * *
>
> And finally, as to the general development of the theory and practice which all this history records; my subject has been Fiat Money in France; How it came: What it brought; and How it ended.
>
> It came by seeking a remedy for a comparatively small evil in an evil infinitely more dangerous. To cure a disease temporary in its character, a corrosive poison was administered, which ate out the vitals of French prosperity.
>
> It progressed according to a law in social physics which we may call the **"law of accelerating issue and depreciation."** It was comparatively easy to refrain from the first issue; it was exceedingly difficult to refrain from the third and those following was practically impossible.

The French inflation of 1791-96 worked very much like the inflation of Germany and Austria in 1919-23. The inducements and delusions which kept it going when once under way were the same, and they are inherent in the process. There is nothing new to learn about inflation. It has had plenty of trials.

Effect Upon Export Products

The producers of export products will find that prices for them are influenced by prices abroad precisely as now. They may think they will gain by the conversion of foreign prices into domestic prices at rates increased by the depreciation of our money, but they are likely to be disappointed in the varied reactions of the markets and the exchanges. If the exchange situation should make foreign prices more profitable to American wheat shippers the foreign markets could be easily gorged with American wheat until falling prices had ended the advantage. British producers have been distinctly disappointed in the results obtained from their country's departure from the gold standard. While the depreciation of their money enabled them to get a bunch of orders at the outset, that kind of competition carried world prices lower and prevented their reaping the expected gain. The competition of depreciating currencies is recognized as the most threatening competition in the world today.

The French Devaluation

A more plausible proposal for inflation than that of cutting wholly loose from the gold standard is suggested by the idea of simply reducing the gold content of the dollar, thus increasing the number of "dollars" that would represent the country's present stock of gold and presumably bringing about a corresponding rise in commodities and other values

measured by gold. It is argued that the country would remain attached to gold as now and that the extent of the change in the dollar. or in other words, of the rise of prices, would be definitely limited. The value of this limitation may be doubted because the course of arbitrary inflation usually is by successive steps, each of which is short enough to be justified by public opinion at the time, and once the policy is adopted of altering the dollar from time to time to suit the opinion of the day there is no reason why the first devaluation should be considered as final. The plan may be interpreted as fixing from the first a definite goal but leaving the movement to it to be determined by natural forces.

The principal argument offered for this plan of devaluation is that France followed it, apparently with satisfactory results. In fact, France adopted it under very different circumstances from those in which we are situated. France adopted the new unit in 1928 as the final act of a policy begun in 1926, and in which the guiding principle was to create a new unit which would conform as nearly as might be to the current value of the currency in gold and the current level of wages and prices in France. In other words, the aim at that time was not to inflate or deflate, but to stabilize and end the task of managing the currency.

The pre-war value of the French franc in United States money was 19.3 cents. It was very much depreciated during the war, and of course the depreciation added enormously to the cost of the war and of the reconstruction expenditures afterward, with the result that the public debt became stupendous, and the amount of currency in circulation was on a like scale. Interest charges and current expenditures were so large that it seemed impossible to balance the budget. With deficits occurring from year to year and the currency still increasing in volume and depreciating, the idea became prevalent that the franc would go the way of the mark, i.e., to the discard. Liquid capital left the country in large amounts. In the summer of 1926 almost a panic existed, the franc sinking to 2 cents. At this point, a coalition cabinet was formed with M. Poincare as Premier, and he was given practically a dictator's powers. He used them ably, but evidently it was hopeless to think of restoring the currency to its pre-war value. The national debt could not be paid on that basis, even with the very high level of prices then prevailing. It is to be borne in mind that no new inflation was proposed by the devaluation. The currency already was devalued and all business adjusted to the devaluation.

The plan created no gap between old and new standards such as business would have to cross in the event of devaluation of the dollar.

Moreover, France did not possess gold enough to serve as backing for the amount of currency outstanding. The country could not return to a gold basis without revaluing the gold stock in relation to the currency. There was practically nothing to do but determine at what rate the franc could be safely stabilized, i.e., at what rate it could be most surely maintained and with the least disturbance to existing business conditions. About two years were taken for careful study and observation, and the rate was then fixed in terms which correspond to 3.9179 cents, and this rate has been successfully maintained. That this was the only course open is evident from the fact that this rate is only about one-fifth of the pre-war rate.

The Position of the United States

The situation in the United States differs from that of France in 1926-28 in that this country has no inflated, depreciated, fluctuating currency imperatively requiring support if it is not to become worthless, but has a reserve ample to assure stability; in France the act of devaluation was in conformity with existing conditions, for the purpose of stabilizing and relieving the country of uncertainty and alarms, while here such an act would change and unsettle existing conditions, creating uncertainty and alarms; and, finally no such inflation of credit or prices has existed at any time in this country as existed in France, nor does the burden of public and private indebtedness here bear any such relationship to our capacity to pay by the long-established standard of value as the debt burden of France bore to its ability to pay at the pre-war standard. There is no similarity in the two cases. With France the change in the monetary unit was unavoidable; with us it would be wholly a matter of expediency, and to say the least there is grave question as to whether the policy would be helpful even to the class in whose behalf it is urged.

In so far as the effects upon business of this method of inflation are concerned, they would be substantially as reviewed above. There would be the same shock to confidence, the same uncertainty as to the public reaction, the same disposition on the part of the individual business man to await definite developments, the same absence of relief from the fundamental problem, the industrial disequilibrium, and all of the other complications.

But let it be assumed for the sake of argument that the proposal could be put through over night, without the delay inevitable in passing both houses of Congress and obtaining executive approval, with incidental agitation and alarm, and that with all conditions favorable confidence would be restored as hoped.

The gold reserves of this country are now larger than they were in 1928 or 1929, and even with the present gold content of the dollar, 23.22 grains fine, are sufficient to support a larger volume of credit than was outstanding in those years, and therefore a higher price level for commodities, stocks and other property than then. It is all a matter of the will to buy, manifested with sufficient unanimity. If the present monetary gold stock of $4,000,000,000 should be revalued in this manner it would become $8,000,000,000, or more than twice as large as in 1928-1929 and with present prices as the basis of a rise the stage would be set for a bull market performance the like of which never has been known. But what would become of the ideal "stability" of which so much has been heard recently from the advocates of reform in our monetary system? So much indebtedness has been cleaned up one way or another, that it would be like beginning all over again, with the whole gamut or cycle of inflation, debt-making, crisis, and deflation to be lived through at a higher pace, ending probably with another devaluation of the dollar! Indeed, why should not history repeat itself more rapidly with the rising tempo of the times?

Prices and Debts Since 1914

The present unit of value of the United States was established by the first coinage act, passed in 1792, was slightly changed by acts in 1834 and 1837 in pursuance of efforts (fruitless) to secure the concurrent circulation of both gold and silver standard coins, but has remained unchanged since the year last named. Prices have fluctuated widely in these years and severe depressions have occurred. Twice, in the seventies and in the nineties, the gold standard was vigorously attacked as having responsibility for depressions, and declarations were earnestly made to the effect that the country was hopelessly ruined unless relief was given by abandonment of the gold standard. It was not abandoned or altered and each time in a few years the country was enjoying a new era of unprecedented prosperity.

Two violent disturbances of the debtor-creditor relationship have occurred since 1914. The first began with the outbreak of the war, and rapidly increased the cost of living. The entire scale of expenditures was raised by the inflation of credit inaugurated by the war.

A large body of indebtedness and of contractural obligations of various kinds, including leases, pensions, bank deposits, insurance policies, etc., calling for payments of fixed sums of money, was outstanding before the war, and of course the beneficiaries of these began immediately to suffer losses in the purchasing power of their incomes. Measured against the cost of living as calculated twice a year by the Department of Labor, an income fixed in terms of money in 1913 had in 1920 only about 46 per cent of its original purchasing power, in 1929 about 59 per cent, and as late as December, 1932, about 70 per cent. Thus throughout all the years since the war-inflation began the holders of such incomes have been unable to realize the values from them that might reasonably have been counted upon, and with few exceptions the principal of the investments could not be realized without loss, which remains true today. A matured life insurance policy will now realize the beneficiary only about 70 per cent of what the same sum would have meant in 1913.

All of this has been and is unfortunate and deplorable, but it has not been suggested that there was any redress. Neither the debtors nor the creditors in this situation foresaw the war or have any responsibility for it. It has been an old custom to have a clause in bills of lading providing that the contract did not insure against losses by "an act of God or a public enemy." And so the vast losses of many kinds resulting from the war and its interference with private business are irremediable. They have to rest where they fell, because they are too great to be remedied. If shifted from one set of people to another they would still have to be endured, and it cannot be presumed that in the ramification of effects the general welfare would be any less affected.

So much for the original disturbance of the debtor-creditor relationship. The second disturbance followed from the first. Throughout the rise of prices, all the way to the peak in 1920, new indebtedness and other contractural obligations were being created. During the rise the losses of those in the creditor position were gains to those in the debtor position, but after prices reached the peak and began to decline the situation was reversed. Losses to the debtor side began to occur, apparently with gains to creditors, although the position of the latter is uncertain. Let it be said at once that these losses are deplorable also. Such wide swings of prices either up or down are very disturbing in business affairs and regrettable for many reasons.

It is now claimed in behalf of the debtors that the value of money has changed, that more commodities are required to discharge a debt than when it was incurred, and that the law should be changed to adapt the dollar to the fall of prices. Granting that prices have fallen, the same logic applied in 1920 would have required that the number of grains in the dollar be increased in order that justice would be done the creditor. That would have been foolish, for there was no certainty that prices would remain where they were in that

year, and they did not. Nor is there any certainty that prices will remain where they are now.

The fundamental truth is that throughout the rise and fall of prices since 1913 the monetary law has been unchanged, hence the law is not responsible for the fluctuations. If, however, the law is now changed in the interest of debtors—and, let it be said, in the supposed interest of justice—the law and the Government will be responsible for the effects of the change, whether they are the intended effects or not. If subsequent developments should show that prices might have moved up, as they had previously moved up and down, without any change in the law, the effect of devaluing the dollar would be to subject the creditor class to further losses. It is one thing to suffer by "an act of God or a public enemy", but it would be another and very different thing to suffer by a deliberate ex post facto change of the public law. The latter, in a matter so important as the standard of value, could not but have unsettling and far-reaching effects.

The Cause of Inflation

It is useless to argue over the abstract proposition that gold is priced in commodities as truly as commodities are priced in gold. It is plainly evident that the great rise of wages and commodities was inaugurated by the war, which created a practically unlimited demand for man-power and the materials and supplies wanted for the war and population, and the demand was backed by practically unlimited credit. Great shipments of gold came to this country in payment for our exports and served as the basis of credit expansion. A competitive demand for labor existed, and wages and the costs of living advanced by a spiral course, the result of attempting to drive the industrial organization beyond its capacity.

After the war gold continued to come to this country, as a result of the favorable trade balance, the fact that this was the only nation on the gold basis, and because the unsettled conditions in Europe prompted transfers for the sake of security. In the four years from December 31, 1914, to December 31, 1918, our gold increased by $1,347,000,000 and in the six years from the latter date the increase was $1,339,000,000, a total of 148 per cent in ten years. Obviously such an accumulation of gold would have been impossible under normal conditions.

It is absurd to say that gold, an inert and lifeless metal, which moves only under some influence outside of itself, had any responsibility for these movements or the price changes resulting from them. It was simply used as something of recognized value, for which the people of all countries were willing to give their products and services, and peculiarly suitable for international payments,—the very facts that have made it first choice as the standard of value among nations. It was used as it has been used in the service of trade since the dawn of history, and if it was used unwisely and harmfully the responsibility belongs to the human directors of its movements. Throughout all the price fluctuations, first upward and then downward, buyers and sellers together made the prices, and down to this time no better method of price-making has been discovered. The human factor cannot establish an alibi by saying that gold did it. If the human factor is to mend its ways, it must recognize responsibility for them.

The Period of Speculation

With the war ended the energies of the American people turned into new channels, and with these extraordinary gold reserves a vast supply of cheap credit was available for use. Development in many lines had been held back and was now released, while speculation, which had been held in check by the war, broke loose upon the wildest career ever known. It began in farm lands, in the middle west, had a spectacular run in Florida, spread into city and suburban real estate and building operations over the country, and gave the final grand performance on the New York Stock Exchange. It is needless to review the follies and extravagancies of the various booms, but one illusion was common to all, i. e., a loss of regard for value based upon utility or earnings and concentration of interest upon current prices.

A special inquiry by the Department of Agriculture in 1920 revealed that the average selling value of all farming lands in Iowa increased by $121 per acre in the five years from 1915 to 1920, and that in the single year from March 1919 to March 1920 the increase was $63 per acre. Something like this occurred afterward in the other fields of speculation. Nor were these the first episodes of the kind ever known. Nothing is more familiar to the students of markets than that the chief influence upon prices arises from the impulses, emotions, illusions and mass movements of mankind. The fact is that in the boom years the people were doing business with bank checks without much regard for any standard of value but market quotations from day to day. They were on a voyage of the imagination, off the earth and away from realities.

The Influence of Debt

Undoubtedly the worst thing about rising prices is the inducement they offer to debt-making. Mention has been made of the rise of Iowa farming lands in 1915-20, and the sequel to that rise is seen in a report issued from Iowa State College in 1932, showing

that the farm mortgage debt was then three times as large as in 1910. It will be agreed now that this is very much to be regretted, even though one may not follow a worthy professor in that excellent institution who begins a recent statement of the farm situation by saying that "the unstable value of money is one of the gravest weaknesses of the economic system." The college figures for that indebtedness show that the principal part of the increase occurred between 1910 and 1920, which was the best ten-year period for getting out of debt the farmers of Iowa ever knew.

The making of debts and prices was a combined operation, the debts supplying the buying power and the latter raising the prices, which in turn created more debt. That could go on for some time under the abnormal conditions which existed following the war, without any relation to the monetary standard.

There is a well known principle of action and reaction in both physics and psychology. A reaction is in correspondence to the violence of the original action, and this has been illustrated by the rise and fall of prices since 1914. Among the theories of Technocracy, a cult which recently has had a fleeting career in the public eye, and whose doctrine seems to have some similarity to the theories of Inflation, one was that the present economic system is responsible for the increase of indebtedness. Any economist worthy of the name will say that such an increase of the body of debts as has occurred since 1914 is not a necessary or normal feature of the existing economic system, but results from abnormal conditions, such as a war or a state of credit inflation which causes people to believe that they can make money easily by going as deeply into debt as possible.

An increase of debt out of proportion to the increase of physical wealth always has been regarded as unwholesome and dangerous, and this country has had numerous demonstrations of its evil effects, invariably related to credit inflation. Such an increase of debt undermines the whole price structure and makes it vulnerable to a pronounced reaction, because it increases the volume of offerings likely to come on the market. A limited amount of farming land can be sold in a given neighborhood in a year without affecting current prices, but if on account of debt or other reasons a very much larger amount is forced on the market, prices may be seriously demoralized, and so it is with all kinds of property when the normal equilibrium is disturbed. It is the natural working of the law of supply and demand. When the normal equilibrium is restored permanent influences again assume control.

In the great disturbance of prices since the war interrupted the normal course of business, the monetary standard has had no responsibility. In so far as it had a part in the inflation it was a subordinate part, controlled by the events of the time, and in so far as it had a part in the deflation it was in the sense that any fixed standard of value sets an ultimate limit upon rising prices and debt-making, and maintains some sort of relations between past, present and future prices, although the use of credit gives great elasticity in these.

Furthermore, price fluctuations are caused by any conditions which disturb the normal equilibrium between supply and demand, as for example the changes in agricultural production caused by the cutting off of Russian exports during the war, the resulting increase of production outside of Europe, and subsequent reappearance of Russia as an important exporter, which broke the price of wheat below $1.00 in Chicago in 1930 and helped to pile up a surplus which has increased every year since. These changes were not related to the monetary standard and have been the principal influences affecting prices of agricultural products since 1914.

The Creditor Class

Throughout all of the boom period there were people who knew instinctively that something was wrong with the heedless debt-making which was adding nothing to wealth-making capacity, and who preferred to invest their savings by such prosaic methods as accumulation at ordinary interest, in banks or by the purchase of bonds, mortgages, life insurance or other outright investments, rather than in margins. These persons were exerting a stabilizing influence, an influence for the normal, constructive methods of making gains. They had no part in building up the topheavy structure of credit and prices which finally crashed. If everybody had followed their methods there would have been no crisis or disastrous fall of prices.

It is not intended to suggest that those who participated in the mass movement were consciously offending against the public interest, or that they are deserving of no sympathy, but a question of public policy is involved. The creditor class is not to be regarded as a group of idle rich who render no useful service. The great bulk of the holdings are individually small, although the aggregate is large. The number of outstanding life insurance policies in force at the end of 1932 is estimated at 65,000,000 (not including industrial) and the amount of insurance in force was $103,700,000,000. The aggregate of savings deposits in all banks June 30, 1932, was $24,281,000,000 and of all deposits $45,390,000,000. The aggregate holdings of the creditor class of course equal the aggregate obligations

of the debtor class, counting in the former only holdings which represent fixed obligations.

All wage and salary-earners are in the creditor position, although not holders of time contracts: their pay is in fixed sums and they would suffer by loss of purchasing power as truly as by rate reductions.

It is natural that some persons, either because they have reached the age which prompts a wish to retire or because their tastes do not incline them to active business, should prefer to lend their capital rather than employ it themselves, and this inclination opens opportunities to others, lacking means of their own. The debtor-creditor relationship is legitimate and mutually advantageous.

On the other hand, with full allowance for the part which legitimate speculation plays in carrying actual risks in the business world, and in stabilizing prices, it is evident that the influence of excessive speculation is anything but stabilizing, indeed a menace to stability. Moreover, the demands of excessive speculation upon the money market raise the cost of capital and credit to legitimate business. The report upon the Iowa land boom referred to above stated that the prices to which lands had been raised were much above any valuation upon which compensating returns could be earned, and that this situation made it practically impossible for renters to become owners with any expectation of paying the price out of farm operations.

These considerations lead to the question whether in the public interest it is desirable that after every boom period in which an excessive amount of debt has been created by fictitious prices, a general release in whole or in part shall be decreed upon all indebtedness, at the expense of the creditor class? To do so would have the effect of loading our public policy heavily in favor of inflation and speculation upon credit, and against the conservative class. In truth the eventual effect would be to destroy credit. The inclination to go into debt needs no stimulus. It is strong enough to be an element of peril in our economic life, and has been the chief factor in every crisis and depression this country ever has had.

The Question of Practical Relief

Nothing approaching equitable treatment of all hardships resulting from the fall of prices is possible by sweeping legislation. Debts were incurred at different times throughout all the period of rising and falling prices; moreover, there have been losses not now represented by debts. Many contracts already have been liquidated by foreclosure, cancellation or compromise, and these processes of settlement are going on daily. It would be most unjust to have a large proportion of the debts settled by concessions on the part of the creditors and then have these creditors mulcted by inflationary legislation. The possibility of this is calculated to hold up settlements. Where there is pressing necessity of adjustments it is usually in the interest of both parties that the terms shall be worked out by mutual agreements.

Interest rates are declining, and with no legislation to disturb conditions undoubtedly will continue to decline, as capital accumulates and seeks safe investments. The lessening of uneconomic speculation will tend to lower interest rates. These conditions will be helpful to debtors as opportunities for renewals or refunding occur, but all depends upon no uncertainty about the monetary standard.

Unquestionably this is a time of great stress and anxiety for many worthy debtors. There is need for cooperation on a large scale to tide over the very real emergency. For the good of all the right policy for the time is one of tolerance and consideration toward those who, because of conditions beyond their control, are unable to meet their obligations. Apparently this is the general attitude of persons and corporations who are in the creditor position. Proper legislation, Federal or state or both, is in order to afford temporary protection against dispossession in meritorious cases. It is not to be thought of that sweeping dispossession of mortgaged homes shall occur, and some legislation seems to be desirable touching the practice of granting deficiency judgments where no really competitive bidding occurs.

A Grave Responsibility

The Government would assume a very grave responsibility in deliberately changing the content of its standard coins for the purpose of altering the relations between debtor and creditor, particularly at a time when conditions are obviously abnormal, unsettled and undoubtedly to a great extent temporary. The Congress would be deciding that commodity prices could not recover by the free play of economic forces, when there is no certainty that this is the case, and the weight of opinion among trained economists is against it. Furthermore, the most serious effect would be to permanently impair public confidence at home and abroad in the monetary system of the United States. If one Congress may change the standard of value on a hasty judgment, to conform to its ideas of whether prices are likely to rise or fall in the future, so may any other Congress. No act of Congress for this purpose ever has been passed in the history of this country. For the first time a precedent would be set for such legislation, and a new and most dangerous factor would be introduced into our politics. It would thenceforth always be in order to propose

changes in the value of the money as a means of regulating prices.

All of the arguments for immediate action are based upon the theory that the present state of prices, industry and trade will be permanent unless legislation is adopted to correct them. There is no sound basis for these assumptions. On the contrary, there is good reason to believe that this depression, like all that have preceded it, will be cleared up by the free play of economic forces if such are not nullified by ill-advised legislation.

The Money Question

The foregoing does not mean that the last word has been said about money, the standard of value, or banking. The standard of value is a subject for scientific study, and international cooperation. The interests of nations are not in conflict upon this subject, for the main object with all is to obtain stability of relationships.

Although the increase of indebtedness in this country after the outbreak of the war was primarily due to the influx of gold, which would have been impossible but for the war, and to the war demands upon our industries, it was very much aggravated by the excessive issues of bank credit for speculative uses. The fact is the expansive possibilities of 26,000 banks with the additional facilities provided by the Federal Reserve system never had been fully comprehended. One of the benefits expected from the Federal Reserve system was that it would afford a central control over bank credit, and the principle of central control has not been discredited, although for several reasons the Reserve Banks were unable to make it fully effective. For one thing, central bank control can be exercised only when the member banks have come to the limit of their own resources and seek to borrow of the central institution, and when gold imports were coming in on a great scale they were of themselves the means of inflation. In the second place, when the Reserve Banks sought the cooperation of member banks in restricting the supply of funds for stock market operations, the restriction caused a rise of interest rates on the New York market which induced the conversion of a great aggregate of deposits into stock exchange loans, and brought money to New York from all parts of the country and all parts of the world. Furthermore, the complex banking situation in this country,with the numerous state banks outside of any central control, and the pyramiding of their credit issues upon the central reserves, presents a problem which must be solved before any effective control over the inflation of boom periods can be had.

It should be borne in mind all the time that the world war was the dominating influence in causing this terrible confusion, and that probably a like situation will not occur again.

Reference has been made to the similar conditions existing during the presidential campaign of 1896, and the similar predictions of disaster then current, followed by a speedy recovery. It has been said that recovery then was due to an opportune increase of gold production, but gold supplies have been increasing faster in the last three years than after 1896. The annual rate of gold production in the world has increased since 1929 by approximately 25 per cent, and the increase of monetary gold stocks in the last two years has been greater than in any other two years of all time. Gold production is now running at a rate well above that of any time in the past, with renewed interest stimulated by the decline in production costs.

The obstacles to recovery are not in the monetary system, and before resorting to attacks upon it—the most dangerous of all subjects for hasty legislation—it will be prudent policy to study other features of the present situation.

The Cause of Disorder

In the December number of this publication the most important condition of prosperity was briefly described as follows:

> All students of the subject recognize that the fundamental condition of prosperity is a state of balance in the various economic relationships between individuals or groups of the population. It is necessary that costs, prices and wages of every kind be in equitable relation with other costs, prices and wages, so that the goods or services offered by each group will exchange on an equitable basis with those offered by others, resulting in a rapid flow of all products into consumption. Goods coming to the market not only satisfy needs but represent buying power for other goods, and there is no source of buying power outside of the exchanges between the various industries and occupations. Full employment, ready sale of goods and a high state of comfort are all dependent upon these exchanges, and hence upon the maintenance of balanced relationships.

The industrial system is a complicated organization which can operate freely only when in a state of order. When by any disturbance it is thrown into disorder, the wise policy is to do what is done for every intricate mechanism under like circumstances, to-wit: make the adjustments that are necessary to put it in order again.

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